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NUMBER I

PROGRESSION IN THE LAND AND BUSINESS TAXES

INTRODUCTION

The prevailing notion of the land and business taxes is that they should essentially be proportionate instead of progressive. But the fact is that the land tax is gradually turning from a tax on products into either a partial property tax or a partial income tax, while the business tax is also assuming the nature of a partial income tax. Thus, these taxes are not satisfied with being proportionate and tend to adopt the progressive element. When a more elaborate consideration is given to the faculty principle as well as to social policy, a greater demand for the progressive element will be felt for these taxes. Although the idea that proportion is sufficient for these two taxes still persists in remaining, there is the unmistakable tendency towards progression. This need has come to be recognised by some scholars, while legislators have utilised this principle in their

law-making. The legislature of this country has been adhering to the old notion of proportion in the land and business taxes and has been quite unaffected by this universal trend of attaching importance to progression. In my opinion, it would be better for this country to abandon its present policy and adopt the progressive principle in these taxes. I shall herein point out the reasons for this belief of mine and shall set forth the methods of the adoption of this principle in taxation.

PART I

PROGRESSIVE RATES IN THE LAND TAX

CHAPTER I

REASONS FOR A PROGRESSIVE LAND TAX

Before taking up the question as to why progressive rates have come to be adopted and are more preferable to the old proportionate rates, I wish to explain why proportionate rates have been hitherto held as proper and reasonable by scholars and lawmakers.

(1). Reasons for a proportionate land tax.

(A). From the standpoint of impartial taxation.

(a). Impartial taxation according to the faculty principle—In the land tax, proportion has been regarded as proper because of the following reasons: first, that tax has been primarily regarded as a real tax; secondly, consideration has been given to the land but not to the person possessing it; and thirdly, each lot was taxed individually and objectively. If a progressive tax is to be levied, it may be based upon the size of the lots. It will result in partial taxation between those possessing a small number of large lots and those possessing a large number of small lots (the burden of the former being heavier than that of the latter), even though the amount of the products or the income therefrom may be equal in both. This is why progressive taxation is

rejected. But this application is wrongly made. The better and right method would be to base progression on the total amount of lands (classified into categories, for instance, as residential lots and field-lots) possessed by each person (or each household). This method too, however, would involve a measure of partiality, if other factors are not taken into consideration. It would not be sufficient to consider the size of land of the same category possessed by a person (or a household) to the exclusion of other factors such as revenue or property other than land; this method would not be entirely just because the person's real or entire faculty is not considered. Let us take the following example. Suppose A receives an annual revenue of 10,000 yen from his lands and that he has no other revenue, while B receives an annual revenue of 1,000 yen from his lands and 1,000,000 yen from his stocks and bonds. Under the operation of a progressive tax, A will be taxed on the revenue from his lands more heavily than B, although his total faculty to pay is much smaller than that of the latter. Again, when both A and B receive an annual revenue of 10,000 yen each, B's revenue from his lands alone being only 1,000 yen, then the operation of the progressive tax would be partial to A whose 10,000 yen revenue is derived entirely from his lands. Instead of adopting such a progressive rate having the possibility of partiality as shown above, one may argue, the more natural and objective proportionate rate should be retained in the land tax.

(b). Impartial taxation according to the benefit principle—In the case of the local land tax, the benefit principle is taken into consideration, and in view of this fact it seems that a proportionate is more proper than a progressive rate. The degree of benefits upon the lands through the growth of local organisations and their establishments varies with different lots, not progressively, but proportionately. Of course, this argument is true only as to the local land tax, and is not true as to the national land tax. Moreover, it should be noted that even in the local land tax the benefit

principle is used as a supplement to the faculty principle, and in consequence occupies a position of much less importance when compared with the latter principle.

(B). From the standpoint of tax technique and in consequence of impartial taxation.

If a progressive tax is to be levied on the entire amount of lands or of the lands of the same category possessed by a person or a household, according to the size of the lands, evasion may be attempted by taxpayers by placing part of their lands in others' names. Nor is there any way in tax technique that can prevent such an objectionable practice, and thus the system would result in partiality and injustice unexpected by the lawmakers. A proportionate rate will do away with such an evil practice on the part of taxpayers, the advocates of proportion will contend. We admit that such evasion is possible. But it should be noted that one would risk much damage by placing his property in another's name, so that the evil feared cannot be so extensive. At any rate, when this evasion is taken into consideration, a proportionate rate seems to be better than a progressive rate.

(2). Reasons for Progression in the Land Tax.

A progressive rate came to be imposed on lands, as we have already pointed out, because of the fact that the land tax has gradually been turned into either a partial property tax or a partial income tax. On the other hand, it may be said that with the adoption of progressive rates in the taxes on wages and capital interest, the same principle came to be applied to the land tax also. This is the historical reason for its adoption in the latter tax. Let us now examine its theoretical foundations.

(A). From the standpoint of justice according to the faculty principle—Although injustice will ensue if each lot is taxed progressively, a degree of justice may be secured by the progressive taxation of a person or a household according to the total amount of land or lands in the same category in his or its possession. A person possessing land

the value of which exceeds a certain point, may be regarded as possessing a large faculty because of that very fact, even though he may not receive any income from other sources. True, it is possible that a person whose land is below that point may receive a large revenue from other sources, and in consequence his faculty cannot be said to be smaller than those whose land are larger but who have no income from other sources. But so long as the possibility remains that persons possessing small areas of land may get only small revenue from other sources too or may get no revenue whatever from other sources, we may conclude that the entire faculty of such persons often is comparatively small. Progressive land taxation or taxation according to the extent of lands, will not be able to estimate the comparative size of faculties as perfectly as when all the faculties are grasped; and in consequence cannot be as completely just and fair as in the latter case. But progression in the land tax will make possible the estimation of the size of faculties to a certain extent, and thereby secure justice in taxation to some degree. One must not overlook the fact that progression in this tax cannot be so just and fair as where the complete personal ability is grasped. Thus, the justice secured by progression of the land tax is a matter of rough estimation; and in consequence the stages of progression should be few in number.

(B). From the standpoint of social policy—As has been stated, the progressive land tax may be explained from the standpoint of the faculty principle with a measure of success,—not a complete success. But when arguments from social policy are added to those from the faculty principle, progression in the land tax will receive a formidable theoretical support. Progression in the taxes on all lands or the lands of the same category possessed by a person or a household will have the sociopolitical effect of preventing the concentration of land in few hands. The concentration of land whether in rural or urban districts into a few hands is highly undesirable from the standpoint of the welfare of

society. The progressive land tax can check this unfortunate tendency, to a certain extent.

It also imposes a differential taxation in favor of the resident landlord over the absentee. Thus, there is a need for specific progression. The burden should be lighter on the peasant than on the owner of tenant lands. In this respect, too, specific progression may be adopted. A differential tax in favor of the lands affected by natural calamities over other lands is also desirable.

(C). From the standpoint of economic policy—Differential taxation is seen between desirable lands and undesirable lands and this results in the adoption of a specific progression. Examples of this discrimination may be found in the comparatively light taxation of improved lands over unimproved lands; in the allowance given to developed or cleared lands for a fixed period of time; and in the lighter tax rate for land developed or utilised sooner than others.

(D). From the moral standpoint—This may be included in that of social policy, but nevertheless forms a separate point of view. To begin with, land is a natural object; it is a gift from Nature as the common property of mankind, and not as the possession of some few men only. Primarily, it was to be owned in common and not to be monopolised by a few specially favoured persons. Of course, the present lands have been improved upon by men and contain human endeavours and capital. When land is sold, its natural value and improved value are taken together. Thus, investment is made upon a land when a person spends on it the money which he has secured elsewhere. By this way, the value of such a land ceases to be merely natural and assumes an artificial character too. But all this change is the result of social systems created by men, so that land itself remains a natural object and thereby retains the character of a gift from Nature. Moreover, land is needed by every one and if it should pass into the hands of a few persons, the latter would be able to control the life of the mass; its concentration therefore must be regarded as high-

ly deplorable. It is desirable to place some limitation upon its ownership; and from the standpoint of social policy, the adoption of a progressive tax is urged. Aside from this question, the moral requirements of man tell him not to pursue economic interests alone, but to live a life in accordance with high moral principles. A man should consider moral doctrines in dealing with the problems of land, and should refrain from gathering large quantities of it into his own hands for his own behalf. When circumstances force him to take possession of a large tract of land, he should use it not for his private interests alone but for the benefit of the public as well, in order that the welfare of the mass may be thereby actually promoted, instead of being jeopardized. Economic and social systems may allow him to possess such an extensive area of land, but he must not forget the moral consequences of such possession. The State should so act and legislate as to promote the moral conception of land possession by private individuals. It must be noted also that the possession by a man of land smaller than a certain quantum would not harm society; but the possession of a large area of land by an individual would be harmful directly and indirectly for other people and injurious to society in general. Thus, the progressive land tax would oblige the possessor of a large tract of land to consider the social implications of his possession, and thereby tend to maintain the social morality of the people.

CHAPTER II

METHODS OF PROGRESSIVE LAND TAXATION

We have seen the reasons for the progressive land tax. We shall now survey the various methods of progressive land taxation.

- (1). The ordinary or inherent progression, that is, when a differential tax is levied according to the amount of

such tax bases as actual products, estimated products or the value of the land belonging to persons or households.

(A). Simple cases—The following are some of the simple methods.

(a). The most proper method is to apply progressive rates not on the total of the tax bases but on the amount of each stage limited at both ends of it by a maximum and minimum. The number of stages should be fewer than that of the income tax or the inheritance tax. This method is most effective against the evasion of the tax.

(b). It is possible to impose a definite monetary amount of tax on the total amount of the tax bases in each stage.

(c). It is possible to levy each rate (in percentage) on the total amount of the tax bases in monetary value in each stage.

(d). First, each abatement is deducted from the tax base of each stage and then a definite tax rate is levied on the remainder. (The abatement is to become less as the amount increases).

(e). It is possible to levy a definite rate on the quotient of the multiplication of the tax base in each stage by the multiple rates ($1/10$, $2/10$, $3/10$ $10/10$).

(B). The imposition of a super tax in addition to a normal tax.

(a). Progression may be reached by imposing a proportionate tax in the form of a super tax according to a tax base which is greater than a fixed amount when taken together with the normal tax (which is levied proportionately according to all the tax bases).

(b). A super tax, which is progressive, may become progressive in a greater degree than the former as a whole when put together with the normal tax (which is proportionate).

(2). Those of specific progression.

(A). Differential taxation according to differences in the management of land.

(a). Discrimination is made in favor of peasant lands and against tenant lands.

(b). Discrimination is made in favor of the resident landlord as against an absentee.

(B). Differential taxation according to differences in the use of land.

(a). Specific light taxation for the purpose of promoting the utilisation of land.

(i). Light taxation on some conditions of utilisation (for instance, when improved land is more lightly taxed than unimproved land, and forest land than farm land).

(ii). Specific taxation in favour of those who have made use of their lands sooner than others in the same position.

(b). Specific taxation against the lands for which government control is deemed necessary.

(i). Land for luxury uses (game reserves for example).

(ii). Heavy taxation on unutilised lands.

(C). Differential taxation on classified lands—Under this system, lands are classified into several categories each of these being subject to a different rate, and the taxes are levied according to the land area, instead of the amount of their value. This is a very rare case, and may be said to be a simple classified rate.

(D). Differential taxation for the purpose of relief: that is, in favor of the lands affected by natural calamities or placed under legal restriction over other lands.

PART II

PROGRESSION IN THE BUSINESS TAX

CHAPTER I

REASONS FOR PROGRESSIVE BUSINESS TAX

Reasons for progressive rates in the business tax may be explained from the two lines of argument, positive and negative.

(1). Negative reasons—denial of proportionate taxation.

(A). Reasons for proportion in the business tax.

In the business tax, each business taxed is taken as real and objective. It is not levied on one's whole capacity to pay, inasmuch as his capacity as seen in things other than his business is not taken into consideration. It is impossible to differentiate the total faculties of taxpayers, and in consequence the undifferential, proportionate tax is justified. It would be unfair to impose a progressive tax, for instance, on products (which are the most proper of all tax bases). Suppose there are A whose sole revenue of 100,000 yen is derived from his business alone, and B whose revenue from his business is 5,000 yen but who derives another revenue of 1,000,000 yen from other sources. It would be unfair to levy a heavier business tax on A and a lighter one on B on the ground that the former's income from his business alone is larger than that of the latter. In such circumstances, it would be better to adopt the simple and natural proportionate rate rather than the artificial and unfair progressive rate.

(B). Reasons for its denial—The view that the business tax which is a real tax or a tax on products which is levied individually and objectively on a real object should be proportionate, is biased and devoid of deep insight. Even when the business tax is based upon such external indications as capital, it is clear that it involves some elements of a personal tax and of the income tax, so much so that it cannot be regarded as a simple real tax or as a simple tax on products. Business cannot yield profits only from objects; it depends on individuals and their efforts. This is why the business tax contains some personal elements. Although it does not consider the taxpayer's revenue from sources other than his business, the fact remains that his business revenue depends on the amount of money he can invest, as well as on his personal efforts, so that the difference in the amount of business revenue implies the difference in the following

factors: first, the amount of capital invested; secondly, individual skill in managing enterprises and in seizing favourable opportunities in conducting business; and thirdly, the nature of the situation in which the business is carried out. Those whose revenue from their business undertakings is greater than others may be regarded as possessing not only greater absolute faculty but also greater comparative faculty. But if an equal proportionate rate is levied disregarding the difference in the amount of revenue, the result is bound to be highly unfair. Of course, there is the shortcoming that in the business tax, also, it is impossible to discover the total personal faculty of the taxpayer because his other revenues are not indicated. So in the business tax, the same degree of progression as in the income tax can not be applied in all cases. But so far as the real and personal elements are indicated in the revenue from business, there should be no hesitation in adopting a degree of progression in the business tax.

(2). Positive reasons.

(A). From the standpoint of faculty indication.

(a). Amount of net revenue—In the same business, the greater one's net revenue, so far as his business net revenue is concerned, the greater will be his faculty not only absolutely but also comparatively. On the other hand, exactly the opposite conclusion may be reached if other circumstances are taken into consideration. But excluding such a possibility, the above proposition will hold water. Generally speaking—and we have to speak generally in dealing with matters in taxation—comparatively wealthy persons are engaged in enterprises that yield big revenue while comparatively poor persons are engaged in those that yield small returns, so that progressive taxation according to the amount of revenue would be largely fair and just. Opposition may be raised against such progressive taxation in the case of corporation enterprises when corporations are regarded as aggregations of many individuals, on the ground that poor men may be shareholders of big corporations and wealthy

citizens, those of small ones. On the other hand, it is equally obvious that the revenues of corporations producing large profits go into the pockets of wealthy persons in comparatively large amounts, while those of corporations yielding small profits are usually received by the poor. At any rate, progressive taxation on business came to receive attention after net revenue had been adopted as the tax base. While its levy was based upon external indications, proportion was thought to be the only method available.

(b). Amount of capital—Difference in the amount of capital may be made the base of differentiation in business faculty. Large capital may be regarded as indicating a correspondingly great business faculty both absolute and comparative, because of the possibility that not only an ample capital will yield a revenue which will be out of proportion, but also the property element plays a much more important part than does the earning capacity. Thus, the amount of capital may be taken to a certain extent as a basis of differential taxation in addition to the amount of net revenue.

(c). Difference in business—The degrees of proportion between the operation of the property element and the earning element are different in different businesses, though the amount of their revenues may be the same; and in consequence there are differences in their faculties, thus justifying differential taxation. Strictly speaking, however, the proportion of the operation of the two elements (property and labor) is so complex that it is almost impossible to put into practice a differential taxation based upon it. If it is to be adopted, it must be based upon a rough classification.

(d). Differences in the forms of undertakings—Differential taxation and in consequence specific progression may be imposed upon corporations and individual businesses, even though the amount of their revenue may be the same and they may be engaged in the same business, because there is a difference in the faculties of the two. In corporations, the property element works to a greater degree than

it does in individual business undertakings. Moreover, the burden of corporations falls indirectly upon individuals and therefore is more endurable.

(e). Size of the location of business—This will not be an issue when the net revenue is taken into consideration. But when external indications are made the basis of taxation, the size of the location of business (city, town, or village) becomes an important factor in the determination of the amount of revenue. But this may be held as a reason against differential taxation. At any rate it cannot be used as an exact basis of taxation.

(B). From social policy—Progressive taxation is more desirable, when looked at from the standpoint of social policy than from the faculty principle. The larger the capital of a business, the greater will be its advantage in competition with other business. The owner of such a business with a big capital has enjoyed advantages in the past, and is likely to continue to do so in a greater degree in the future, so that should he be subject to only proportionate taxation, it would be possible for him to oppress the weaker competitors with impunity. Thus, social policy demands that there should be some degree of progressive taxation.

(C). From economic policy—Protection is thought desirable for a certain business to a greater degree than in other businesses, from the standpoint of economic policy, thereby constituting a good reason for progressive taxation. It may be said, for instance, that the profit of commerce is greater than that of industry, and for this reason the former should be taxed more heavily than the latter. But aside from this matter, there are some industries whose development is especially desired. This is so in the case of export industries, basic ones in particular. In a country like Japan where the improvement of the nation's international accounts is one important point in its economic policy, the special light taxation of basic export industries is highly desirable.

(D). From tax technique—Primarily, the business tax

is intended to be a direct tax by the lawmakers and as such should not be shifted, and if shifting is held unavoidable, it should be limited to as small a degree as possible. And, there is the tendency to make the shifting to consumers and to the recipients of small revenues, but not to those of big revenues. It is evident, then, that the shifting of the business tax is very undesirable from the standpoint of social policy. When a tax is proportionate, there is a greater possibility of shifting than when it is progressive. When the rate is proportionate, the business tax is regarded as the same as a consumption tax and the amount of the tax is included in the business expenses in order to be shifted on. But when the tax is progressive, the burden on business men will vary, and consequently the shifting of the tax would be carried out only to a slight degree.

(3). Points that should be taken into consideration in putting progression into practice—All the reasons in favour of progression in the business tax have been presented. I shall now set forth the points that ought to receive attention if adopting the system.

(A). Inclusion of the benefit principle—All the reasons given above for progressive taxation are derived from the faculty principle. But in the local taxes, the benefit principle is included and this may be cited as a reason against the adoption of progression in the business tax, because under the benefit principle revenue is derived in proportion to the degree of benefits received. But this does not mean that the benefit theory is the only principle on which local taxes are based. It is included in addition to the faculty principle, so that progression cannot be rejected on that ground. So long as the benefit principle is included in the local taxes, it is proper that progression, if adopted, should be somewhat tempered.

(B). Kinds of tax bases—When the amount of net revenue is taken as the tax base, the size of faculty is best shown, and thus the reason for progressive taxation under the circumstances has greater force than when external

indication is adopted as the base of the tax. When a tax is based upon the amount of capital, the reason for progressive taxation are well supported from both the faculty principle and social policy. But when the gross amount is made the basis of taxation, there would be no correspondence between it and net revenue, and proportion would be more desirable.

(C). Easiness of evasion—Primarily, business revenue, especially net revenue, is difficult to reach, and therefore it is easy for the taxpayer to evade taxation. The evasion may be limited within a small compass under proportionate taxation. But progression will encourage evasion on the part of the undertakers of big business enterprises. Thus, progression is justified in theory but involves this technical difficulty of tax evasion. However, there is the possibility that progression would discourage tax evasion among small business men, and we know that corporations are required by law to publish their business accounts. This may make up the defect just referred to.

CHAPTER II

METHODS OF PROGRESSION IN BUSINESS TAX

We have seen the theoretical reasons for adoption of a progressive taxation on business. We shall now consider the methods of adopting it. The following may be considered :

(1). Appropriate methods.

(A). Ordinary or inherent progression.

(a). Progression according to the amount of the net business revenue.

(b). Progression according to the amount of business capital.

(B). Specific progression.

(a). Differential taxation according to kinds of business.

In this system, differentiation is based upon the amount of property elements contained or on the degree of the need of financial protection from the standpoint of economic

policy. In actual practice, the adoption of no great differentiation would be possible, and it is bound to be appropriate.

(b). Differential taxation according to the forms of undertaking. Corporations are taxed more heavily than undertakings by individuals.

(c). When progression is based upon the size of the location of business especially in the case of the license tax. This is not true in the case of the new business tax according to business revenue. But it was adopted and advocated in the old business tax according to some external basis. It may be regarded as a simple classified rate.

(d). Differential taxation according to the percentage of the net revenue to capital. This is justified from both justice in taxation and social policy, but while it can be adopted in the case of corporations, it cannot be applied to individuals, so that there will be injustice between them,

(2). Inappropriate methods.

It is not proper to adopt progressive taxation when external indications are used as the bases of taxation. Such external indications, as gross revenue, rental value of buildings used for business, amount of wages paid, etc., cannot be considered fair bases of progression. Rental value may be said to be proper as the base of the dwelling duty, but not as the base of the business tax.

CONCLUSION

Summarising the foregone arguments, it may be said that the wellnigh universal objection to the adoption of progression in the land tax and the equally universal favor for proportion in the same tax, after all, cannot be held as tenable, and that there are many reasons for the adoption of a progressive tax the degree of which should, however, be lower than that of the income tax or the inheritance tax. The main reason for its adoption is found in the faculty principle, although it may be justified from the standpoints of economic policy, social policy as well as public morality.

We have seen that there are various methods for the adoption of progression in the land tax, and that it may be adopted not only in its inherent form of progression according to such tax bases as revenue, productive capacity, and the amount of land value, all of which are the usual bases of the land tax, but also in the form of specific progression according to various other considerations.

Proportion is generally regarded as proper also for the business tax, but closer enquiry will reveal that, when net revenue or the amount of capital is taken as tax base, progression will be found to be more appropriate. It will be justified from the standpoint of the faculty principle, social policy, or tax technique. Progression is also desirable when viewed from the standpoint of economic policy. There is much room for the adoption of progressive taxes on business, and specific progression may be adopted according to various reasons, in addition to the ordinary progression based upon net revenue and the amount of capital. These methods of progressive taxation are already found to be used in various countries and the reasons for their adoption tend to increase in forcefulness.

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